

## CONTENTS

IT'S HAPPENING IN NILES <i>By David J. Luck</i>	1
CURRENT MICHIGAN BUSINESS CONDITIONS	6
THE LONG LOOK AT STATISTICS <i>By Lawrence Drake</i>	9
A LA CARTE MEALS FOR BABY <i>By Anne C. Garrison</i>	13
THE BLOCKAGE FACTOR IN STOCK VALUATIONS FOR FEDERAL TAX PURPOSES <i>By A. E. Grunewald</i>	21



BUREAU OF BUSINESS RESEARCH  
School of Business and Public Service  
MICHIGAN STATE COLLEGE  
EAST LANSING

## A Promise and a Threat

**CONSIDER THIS PREDICTION:** for every 10 students in Michigan colleges today, there will be from 17 to 22 by 1970. This is the careful forecast of the Michigan Council of State College Presidents. You may have seen these figures in your own newspaper, which printed them as important information for every citizen.

To Michigan's state universities and colleges, and to every Michigander, this is a good promise of the future. The more who are educated to live rich and useful lives, the better for everyone. To the educators it means expanded opportunities to serve, even wider than the far-reaching services of the Land Grant Colleges that were commemorated on Michigan State's Founders' Day, February 12. Yes, there are fine potentialities in education's expansion in years ahead.

This tremendous growth in demands on Michigan's colleges must, however, be viewed with mixed emotions. Each of the state-supported institutions now has about the capacity of students for present faculty and facilities. The threat, implicit in this future acceleration of demand, is that we might be overwhelmed unless the colleges can expand sufficiently. If you ponder the doubling of the physical plant of one of our state colleges, 15 years is a short time for that accomplishment. And if you consider that the teaching profession is scarcely able to provide replacements to maintain the present size of college faculties, you will know that doubling these staffs with qualified teachers will be even more difficult.

Such a threat faces college administrators today. And surely anyone who wants to maintain an adequate quality of education cannot be indifferent to the threat. What can the citizen do about this? (1) He can accept willingly the costs borne by Michigan's people of this imperative expansion; (2) He can tell his legislators that he welcomes their farsighted efforts toward rapid expansion of our colleges; and (3) He can encourage young people to give serious thought to careers in college teaching, a fine profession with a great future.



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*"Let your discourse with men of business be short and comprehensive."*

(George Washington's *Copybook*).

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# IT'S HAPPENING IN NILES

By DAVID J. LUCK\*

*In days like these, when our state continues to grow faster than the nation as a whole, our communities — especially our schools — show the strain. Spring cleaning time is a good time to think of shining up the town we live in. Here is the encouraging story of one community's success in this endeavor.*

## Scene One (Highly Improbable)

The curtain rises on a bridge table one evening in 1945.

Two Niles couples are having a neighborly game, which has reached the familiar stage when conversation gets the upper hand of the wifely element of the party. Looks like the ladies are going on for some time, so their husbands have got started on a subject of mutual interest: the awful state of the school buildings in town. This topic is always good for twenty minutes of civic indignation. Something ought to be done, they agree: someone ought to do something about it — three schools, right in Niles, built before the Civil War! Two schools, inside the city limits of a fine Michigan town, still one-room structures in the middle of the twentieth century! Nobody caring enough to turn out for school elections, either — there were only eight voters at one of the last ones. Yes, someone ought to do something . . .

Plenty of social conversations were running on like that in Niles, ten years ago. Just bridge table talk, you think, and unlikely to lead to anything? That is usually the case when social indignation gets mixed up in a social evening. The difference in this case is that such talk led to action: concerted social action, well-directed, sustained, enlisting a wide segment of the civic-minded. Those two men at the bridge

table became the nucleus of a committee of twenty-five that was soon engaged in vigorous agitation. Candidates were put up for the school board, and defeated. The committee, not daunted by failure in its first round at the polls, elected two members the next year, and triumphantly seated a majority of its candidates in the following election.

The results have been phenomenal. New school buildings have replaced old ones in every part of the city. When the current building program is finished, nine of the twelve schools will be under ten years old. Such changes are costing a good deal, as you would expect; but the seven million dollars involved was voted in several well-supported bond issues, the last one having been favored by the citizens by a majority of  $3\frac{1}{2}$  to 1. Nobody is dragging his feet in Niles, you'll agree.

Nor is this likely to be a grand theatrical move that will gradually yield to familiar social apathy. Intelligent steps are being taken to assure a continuing improvement. P.T.A. meetings draw crowds of 500; there are public information meetings and bulletins are published; the Citizens' Advisory Committee on the school problem is well-informed and active. Needless to say, a concerned citizenry is a more important factor in education than is the best of physical equipment — and such concern means, among other things, that the physical equipment will be forthcoming.

\*Dr. Luck is head of the Bureau of Business Research and Editor of *Business Topics*.

### Face-Lifting

Those two bridge players could have taken up almost any aspect of the public life of Niles ten years ago and found plenty to criticize. The downtown area, for instance, was suffering from a shortage of parking space. The local stores were also inadequate to the city's needs: there was, for instance, not a single men's clothier. One move went far to fill both these deficiencies, when a merchant came out from Ann Arbor to open such a store and to beat the drum for his own particular civic project, a parking development like the fine one in his former home town. He buttonholed everyone who would listen, put on a one-man campaign of public addresses on the subject, and found receptive ears in a city that was awakening to civic consciousness with its success over the school question. Next success, largely due to his efforts, was a program of public parking lot development, culminating in today's five convenient parking areas. Now you can actually park and shop in downtown Niles: perhaps it is no coinci-

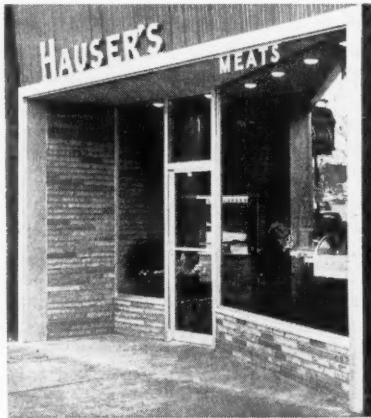
dence that two more haberdasheries have opened since that first one.

Like a river in flood, public awareness continued to wash down the high banks of indifference and unawareness. The next improvement was an aesthetic one, but also very good for business. The Kawneer Company, which is one of the country's leading manufacturers of storefronts, took a good look at hometown facades and found them anything but modern. Together with the merchants, they staged a campaign for a more beautiful business district through remodeling of exteriors. For three years these face-liftings have been going on at the rate of one every month, and by now you'd look far to find a more attractive main street.

This flood of improvements also involves a flood of light, for last year an installation of modern street lights in downtown Niles made it possible to see the spruce new aspect much better than anyone had ever seen the shabbier old-fashioned one. An obvious question arises: does all this pay off? What has the effect been upon busi-



Face-Lifting in Niles: Before



Face-Lifting in Niles: After

ness? Well, there were seven vacant stores in the business district a few years ago, while today there is only one.

Among other changes in the nature of public works are included the two huge water storage tanks, expensive but necessary improvements. Better lighting extends beyond the city as well as inside it, with improved installations illuminating US-31 to the south. A considerable hospital expansion is under way too.

### **Studying Niles**

One of the most invigorating changes of all had nothing to do with physical equipment, but rather with a city's most valuable asset, the intelligence and special knowledge of its citizens. Some of the leading members of the Chamber of Commerce envisaged their part in the city's rebirth as one of study and planning. The Chamber appointed an Economic Development Committee, truly representative of the various abilities and skills of an American community. Its members include a doctor, a banker, the secretary of a charitable organization, a manufacturing executive or two, a filling station operator, a nurseryman, the city attorney and others.

Following plans developed in conjunction with Michigan State College, this key group broke down every phase of the city's public life. Exhaustive study of each aspect in turn enabled them to draw up a comprehensive report to be presented at the annual Chamber of Commerce outing.

### **Scene Two (Also Improbable)**

The bridge table was an unlikely start for such a realistic program of improvement. The next phase opens

just as improbably, with a public address at an annual organizational function. It is June, 1954, and the members of the Chamber of Commerce have had a pleasant afternoon of golf culminating in an excellent smorgasbord. What follows next is the unlikely part: an after-dinner speech that not only keeps its audience awake after eighteen holes and herring salad, but even incites them to enthusiastic response in terms of further actions. David Miller, the Chairman of the Economic Development Committee, presents his report to the Chamber of Commerce.

### **Area Planning**

For every phase of this report, Mr. Miller was prepared with maps, charts and recommendations, the result of laborious study by his devoted committee. This amounted to a community inventory of a most thoroughgoing kind. Interest grew among the members of the Chamber as he spotlighted phases of progress or revealed dark areas where serious civic needs still existed. Before he was finished it was apparent to all his audience that this was a lucid and memorable presentation, and that such economic inventories, periodically prepared, could make a vast difference to any city, and especially to one that was, like Niles, already pulling itself up by its bootstraps.

One point was repeatedly underscored in this report: civic troubles don't end at the city limits. The entire Niles area, extending far outside that artificial boundary, entered into every phase of present problems and future planning. Unity of city and township was the theme of that well-delivered and sympathetically received talk, at the end of which the Chamber mem-

bers responded not only with applause but with a resolution to continue the economic planning, in terms of the entire area.

The present phase of the remodeling of this highly-aware community is the engaging of support of all the people of Niles and the area around it. The groundwork for area planning has proceeded well. The story is now to be carried to the public largely by means of a motion picture dramatically presenting the civic needs. The local photographer who now is completing it is both competent and deeply interested as a citizen. With bookings before various groups for weeks ahead, this film will have a busy time\*.

When the need has been sold to the public and the program authorized, specialists can be set to the task of planning the greater Niles of the future. Their blueprints can be brought to actuality through the same means as Niles' other civic improvements: a demand arising from the citizens and pushed by vigorous citizen groups.

#### **A Worthwhile Example**

While this story is not unique nor even sensational, it is certainly not commonplace. There is still a long way to go before the community reaches its ideals, to be sure, but how far has your own community gone in the past nine years? One needs no great perceptive powers to see vital needs in every town — needs that are not receiving action or even attention. These provide challenges that none of us wants to ignore. The question is, what can the plain citizen do?

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\*Tip to interested communities: it might be possible to borrow this to assist in study of your own town's improvement program.

At least a beginning to finding the answers is right here in the story of Niles — a story that is "improbable" only because a group of people up and did what the rest of us talk about doing.

#### **Implementing Your Own Ideas**

The ideas for civic improvement that you and your friends develop over the card table or at any other social gathering *can* be realized. It may take years of plugging, but most significant progress takes such tenacity.

Progress for the community should not be conceived and obtained in haphazard fashion. The character and magnitude of its needs can be inventoried, whether by the work of interested citizens or of outside specialists employed for the project. Only such a comprehensive inventory can show the way to a suitable community program, and this project will generate a good deal of interest in your city's needs.

Chambers of Commerce should not be confined to furthering the interests of the businessman exclusively. Today's successful chamber of commerce is seeking and promoting activities that benefit the whole community. Every citizen should be exerting his efforts toward bettering his town or city, and he may work through several community institutions. The chamber of commerce has a logical, perhaps undeniable, role in the community effort. *Unfortunately* too many chambers of commerce tend to be undernourished or apathetic, but they could be just as vigorous as their members will make them.

*Business Topics* hopes that in 1955 many Michigan communities will copy or improve on the story of Niles.

## Do You Know These Michigan Towns?

*Recent questionnaires indicate that this is just about your favorite feature. We can go on with it indefinitely, as long as the citizenry furnishes us with towns, and with curious facts about them. Warning: we may use the same town more than once.*

1. The foresighted settlers had their laws and by-laws all drawn up for their new home before they even reached this country. Nothing daunted by starting their Michigan lives in wooden sheds, and being harrassed by malaria and physical hardship, they survived and prospered. Their descendants may have made your hall clock, your office desk, or your coffin.
2. There are only three federal Indian reservations east of the Mississippi and one of them is just east of here. Oil and petrochemicals account for a great deal of the local industry. The geographical center of the Lower Peninsula, and the oil capital of Michigan.
3. "If you have tears, prepare to shed them now". This is the onion capital of our state. It does not contain that tomb of its namesake president.
4. Peanut butter and knotty pine furniture and power shovels are all produced here; programs of school building, hospital improvement and youth service are nationally known. As the state's second largest distribution center of petroleum products, this city is readying itself to take full advantage of the Seaway, with plans already approved for a 24-foot channel.
5. The temperature, which never drops to freezing, is like a fine May day all year round. There is not a day when fresh strawberries cannot be served, and enormous roses sell for about 5c a dozen. The world's best fish, too delicate to be shipped, are sold in the market here. Local industry includes weaving, wood-turning, and sitting around in the sun.

*(Answers on page 28.)*

### REDDER THAN THE ROSE

If you think our cover is red, you should have seen our faces after publishing the January issue. *Business Topics* had barely got out of the postman's hands before loyal readers were pointing out our errors. Herewith we list last month's bloopers.

- 1) Lawrence S. Ritter was mulcted of credit for the article on John Maynard Keynes. This is the second time we have done this to Dr. Ritter. Cause of error: two people in the Economics department have the same initials.
- 2) Those babies in *A Child's Garden of Statistics* are born at the rate of one every eight SECONDS (instead of one every eight minutes), giving us 60 times as many babies as we thought we had. For a business magazine, this represents rather a large mistake. It means that the outboard motors and chewing gum which we affirmed were ten times as plentiful as in 1928 now have to go six times as far. The doughnuts will all have to be divided by 60, too.

Our apologies to Dr. Ritter and 3,933,334 babies\*.

\*Someone had better check this, too.—Ed.

## Current Michigan Business Conditions

The new year in Michigan has continued the upturn that characterized the final months of 1954. With record automotive production and with the end of a period of general inventory adjustment in non-automotive lines, the overall picture is that of a strong economic condition for the early part of this year.

Bank debits (checkbook spending) for the various urban areas of the state reflect the general upturn in business activity that Michigan has enjoyed in the last several months. In all centers, except Lansing, this index of business activity reflects more favorable business conditions than a year ago.

Retail business broke all records during December, decidedly reversing the decline that characterized several previous months. Sales tax collections (representing business of the previous month) of the Department of Revenue were more than 4 percent above the best previous December, that of 1953. Preliminary figures indicate that both December and January sales were substantially above the previous year's record.

Department store sales were generally off from 1953 levels during most of 1954 throughout the state, except in Lansing. In all metropolitan areas, December sales increased substantially, with about half them reporting department store sales exceeding December, 1953. January also proved stronger.

Electric power consumption in this state also was on the upturn in the final months of the year, generally exceeding comparable figures for 1953.

The production of automotive vehicles hit all sorts of records during December, January and February. December factory sales of 766,170 units was the highest December figure in history, and was exceeded only by June and August of the record 1950 year. January followed with 726,108 units, the highest January on record. Preliminary figures indicate that February's production was 676,060 cars and 62,489 trucks and buses. Although truck and bus production was below 1954 figures, February 1955 exceeded last year's total vehicle production by more than 200,000 units and exceeded the previous February record of 1951 by more than 120,000 units.

For the state as a whole, January's employment was at near record levels for this time of year, being exceeded only by January of 1953. The post-Christmas layoffs in non-manufacturing activities were lighter than usual and were partially cushioned by a moderate volume of additional hiring in manufacturing plants. The most significant improvements have been in the Detroit area.

Bank Debits	Bank Debits			Percent Change from		
	(thousands of \$s)		Jan. '55	Nov. '54	Dec. '54	Jan. '55
City	Nov. '54	Dec. '54				
Adrian .....	18,904	22,111	21,135	+ 5.4	+ 10.2	+ 11.9
Battle Creek .....	63,032	71,746	70,574	+ 4.0	+ 3.1	+ 8.1
Bay City .....	44,265	48,736	45,518	+ 5.6	- 4.9	+ 7.5
Detroit .....	4,633,596	5,759,314	5,466,270	- 4.7	+ 1.3	+ 12.1
Flint .....	139,875	179,345	163,925	+ 10.8	+ 29.1	+ 22.5
Grand Rapids .....	282,157	314,175	290,859	+ 11.6	+ 10.7	+ 8.2
Jackson .....	81,378	92,759	88,531	+ 9.9	+ 14.5	+ 11.7
Kalamazoo .....	110,457	127,101	115,454	+ 10.9	+ 9.6	+ 9.3
Lansing .....	123,100	153,268	132,698	- 17.9	+ 0.7	- 7.7
Muskegon .....	69,043	79,870	76,924	+ 6.0	+ 1.4	+ 2.8

CURRENT MICHIGAN BUSINESS CONDITIONS

7

Port Huron .....	34,329	38,049	38,114	— 1.5	+ 5.2	+ 13.7
Saginaw .....	101,502	121,990	102,660	+ 7.6	+ 10.3	+ 8.1
Escanaba .....	10,151	10,869	10,941	+ 7.9	+ 5.7	+ 11.4
Marquette .....	10,974	11,552	10,950	+ 14.3	+ 8.7	+ 5.6
Sault Ste. Marie .....	11,846	12,772	10,497	+ 19.8	+ 17.4	+ 4.8

Source: Federal Reserve Banks of Chicago and Minneapolis

Department Store Sales	December, 1954	1954	January, 1955		
	Percent change from	vs.	Percent change from		
	Nov. '54	Dec. '53	Dec. '54		
Battle Creek .....	+41	— 3	— 9	—54	+17
*Detroit .....	+44	+ 6	— 3	—56	+10
*Flint .....	+49	+ 3	— 2	—56	+12
*Grand Rapids .....	+50	— 1	— 4	—58	+ 4
*Jackson .....	+73	0	— 7	—62	+17
*Kalamazoo .....	+59	+ 4	0	—66	0
*Lansing .....	+56	+15	+ 7	—58	+ 8
Muskegon .....	+70	+ 4	— 7	—61	+14
Port Huron .....	+50	— 8	—10	—67	+ 1
*Saginaw .....	+36	— 2	— 7	—53	+ 8

\*Metropolitan areas

Source: Federal Reserve Bank of Chicago

Electric Sales in Kilowatthours	KWH Sales in 1954			Percent change from previous year		
	Oct.	Nov.	Dec.	Oct.	Nov.	Dec.
Residential .....	448,564	470,946	506,995	+11.2	+11.2	+ 9.0
Commercial .....	271,641	270,205	287,008	+ 7.7	+ 4.6	+ 6.3
Industrial .....	722,759	793,310	820,674	— 1.0	+13.0	+16.8

Source: Edison Electric Institute

**Motor Vehicle**

Factory Sales from Plants in U.S.	Factory Sales			Percent Change from Year Ago		
	Nov. '54	Dec. '54	Jan. '55	Nov. '54	Dec. '54	Jan. '55
Passenger Cars .....	498,248	669,936	636,242	+31.5	+71.9	+40.0
Motor Trucks and Buses	89,537	96,234	89,866	+20.9	+ 1.2	— 6.9

Source: Automobile Manufacturers Association

Non-farm Employment	State of Mich.	Detroit Met. Area	Flint	Grand Rapids	Lansing	Saginaw	Upper Peninsula
Nov. 15, 1954 ..	2,462,000	1,383,000	133,100	166,800	76,000	56,600	81,000
Dec. 15, 1954 ..	2,493,000	1,410,000	134,600	117,700	77,600	56,800	79,600
Jan. 15, 1955 ..	2,476,000	1,402,000	135,700	116,800	76,800	55,900	77,400

Percent change from year ago:

Dec. 15, 1954 ..	— 1.4	— 1.9	+ 7.3	— 1.3	— 2.5	— 0.5	— 3.6
Jan. 15, 1955 ..	+ 0.4	+ 0.7	+ 6.6	— 0.4	— 0.8	— 1.2	— 3.9

**Total Unemployment**

Nov. 15, 1954 ..	164,000	100,000	3,000	4,900	3,500	1,800	9,200
Dec. 15, 1954 ..	149,000	85,000	3,500	4,700	3,100	1,900	10,400
Jan. 15, 1955 ..	153,000	86,000	4,300	4,900	3,000	2,200	11,800

Percent change from year ago:

Dec. 15, 1954 ..	+ 8.0	+ 1.2	0.0	+135.0	+14.8	+18.8	+40.5
Jan. 15, 1955 ..	—13.1	—19.6	+16.2	+53.1	—21.1	+10.0	+32.6

Source: Michigan Employment Security Commission

## CONFIDENCE AND PROSPERITY

*The following interesting remarks are quoted from a broadcast given on January 3, 1955 by the well known journalist and economist Henry J. Taylor, as part of a series "Your Land and Mine" presented by General Motors. Reprinted by permission.*

*Announcer:* Mr. Taylor, last week you spoke of the immense buying power now in folks' hands. How is this translated into purchases of one thing and another?

*Taylor:* Peoples' confidence in the future has a lot to do with it. The potential buying power is immense. In fact, although only about 7% of the people of the world live here, the purchasing power of the American people tonight is greater than the purchasing power of all the people of Europe and Africa and Asia *combined*. Yet, we don't have to buy a lot of things we do buy if we are frightened about the future, which is where confidence comes in . . . About 40% of everything the nation buys is estimated to be postponable if we are afraid to buy. Only about 60% of our national purchases are absolutely essential, and not postponable, as food is not postponable.

Therefore fear itself can cut down on our employment everywhere. It can create a tragic chain reaction . . . Thus the American public's psychological attitude of confidence or fear is of enormous importance. It is important to a degree unique in the world because the way we live is unique.

In Communist Russia, for example, the public's psychology — the Confidence Factor — is not important. The absence of it cannot bring on a slump. The people are permanently slumped. Practically nothing a Russian buys is postponable. He's living at the bottom of a depression all the time. Communist industry today is producing less than one pair of shoes a year per person for the population.

Even in France, only about 5% of the public's buying is postponable. The psychology of the French people has only a small effect. In England only about 15% of British buying can be deferred. 85% cannot. Psychological attitude has relatively little to do with British buying.

*But to be fearful here is fatal to us all.* Thus people's confidence is a tremendous factor in maintaining each others' sales, jobs, production and everything that makes the wheels go round.

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## THE INVASION OF EUROPE

The Dow Chemical Company, of Midland, has just received permission from the Netherlands Minister of Economic Affairs to establish a wholly-owned subsidiary company in Rotterdam. The enterprise, on which building will begin immediately, will have its own tank storage, warehouse and dock facilities. Among the products the firm plans to process are styron (Dow's familiar expanded polystyrene plastic), magnesium alloys and a number of other chemicals now in the stage of economic study. Some of the new Dutch personnel will be sent to Dow plants in this country for special training in production, technical service and sales functions.

# THE LONG LOOK AT STATISTICS

By LAWRENCE DRAKE\*

*Some cautions to keep in mind, the next time we use others' statistics.*

Everybody today is a user of statistics. As a plain citizen, you are showered with statistics on social and political trends, the effects of smoking cigarettes, and many another matter. If you are a businessman, your use of statistics is more than an every-day matter, being an important factor in the success of your operation. My experience with statistics has been a wide one from two viewpoints: formerly in direction of the research work for a large food chain company, and in recent years as an editor using and evaluating data of all sorts. In my personal experience in using statistics and in answering the inquiries that pour upon the editor's desk for business facts, I have become tremendously impressed with the troubles we get into as we try to use statistics. The matters that I am going to discuss are bread-and-butter problems for nearly every businessman, and although the examples cited naturally are drawn from the great business of food retailing, you can find countless similar cases in any field that you care to name.

## Observation is So Limited

There probably was a time in the primitive stages of business development when the manager or owner could operate successfully simply on the basis of what he saw and remembered. Certainly this no longer applies in food retailing, particularly among the chains.

\*Mr. Drake is the Editor of *Chain Store Age*, Grocery Edition. Adapted from an address at Michigan State College.

There are so many food chain stores that a person would have to visit approximately 550 of them every week for a full year to see them all. Even if a man could cover this impossible number of stores, by the time the year was over, one-fifth of the stores would have been remodeled or replaced, and so his information to that extent would be out-dated.

One of the traditions in food retailing was of the late John Hartford, president of the A & P stores, always popping into a different store on Monday morning. If Mr. Hartford had intended by this procedure to see all of the stores in his company, it would have taken eighty years. This inability of supervising an operation by personal observation is not true of the largest chains only. Consider an acquaintance of mine in Florida who operates 23 stores. He tries, he says, to check every store once every three months, and that is about the best he can do.

What I have been saying here about food chain stores of course is true of any large and scattered company, whether it be Western Union or the Standard Oil Company. Yet it is also true of nearly every business enterprise. If they are going to be successful, their operators must use, and use successfully, both internal statistics and data gathered outside of the walls of the firm itself.

## The Place of Statistics

Hence statistics and research records are the only way to keep in touch with

the details. They must be interpreted in all kinds of control operations and management decisions. Yet statistics alone are enough to unhinge the mind unless the user knows how to apply them properly: as a *supplement* to the observation and the experience of management. There may still be some die-hards who say that there is no reason for bothering with statistics since if you live long enough you will have enough experience, but I doubt that anyone will ever live that long.

To illustrate the proper use of statistics, I should like to cite a relatively new book, *How to Lie With Statistics*.<sup>1</sup> Its author, Darrell Huff, believes that someday statistical thinking will be as necessary for efficient citizenship as the ability to read and write. His thesis is that statistics are not always exactly what they seem, and this can be brought out by many examples in my own field alone.

Let us consider what seems to be a simple question, "What were the food sales of food chain stores in 1953?" That is one that I should certainly be able to answer because I am widely quoted on just that point, but the best I can do is to demonstrate what a tough question it really is. There is an index of the sales of food chains in the nation published by the federal government, which is the best thing of its sort that we have. I used to have the illusion that it represented reports of all the food chains every month. Yet in heading a market research department, I could not get that index to tie in with my figures. Sometime later I checked with that government department and found that the sample consisted of a certain percentage of food chain stores that was inadequate in regard to many

factors. In fact, the total size of the sample represented fewer stores than were found in one food chain organization alone. And another question on these figures occurred after I had become an editor when I met an editor of a magazine representing independent stores, and we confessed to each other that we could not reconcile our figures to that index. We were disturbed to the extent that we went down to Washington and found that there had been a slight error in procedure resulting in a minor adjustment of 1.6 billion dollars.

To get down to smaller figures, consider the sales of a particular chain company. This firm's annual report has been audited and is correct to the last penny. Yet I will still state that you have to think about what went into that figure of the firm's sales before you use it, or use any other figure in that report. For example, they state that they have made so many million dollars worth of sales, and they also tell us that they have a certain number of stores. It might seem obvious to you that to get the sales per store you simply divide it by the number of stores. This is simple, but it does not work because this particular organization has several times as many sales routes as it has stores, but they throw all the sales into the total figure. Another chain has the same situation, but sometimes they include the route sales in the total and sometimes only the store sales. For another chain you have to recognize the fact that their sales figures include their stores in Canada, sometimes, and other times they do not. And so you have to know what goes into these figures before you can make sensible use of them.

#### Perils of Surveys

In running any business you have to make use of some data that are gath-

<sup>1</sup>Published in 1954 by W. W. Norton & Company, New York. Quotations by permission.

ered from outside; and if your business is one that deals with the public, quite a number of surveys must be utilized. To see possible dangers in surveys let us look at a very simple question surveyed recently by a large research organization in the food field. A question asked of several thousand women was, "At what time of day do you shop for groceries?" A majority of them replied that they shopped between ten and twelve. The only trouble with this is that you can put a clock on the cash register tapes in almost any food market and find that the peak for that store lies between three and five in the afternoon, when the little lady is attempting to beat her husband home with a couple of pork chops. What must have happened — when some interviewer asked her when she shopped for groceries, she could not admit that she failed to get out at a respectable hour in the morning and do her shopping. Fact and statement do not necessarily coincide.

More often perhaps the figures in a survey are right, but you ought be careful in the conclusions you reach from them. A manager of a retail organization told me recently that he was building a great sales program based on consumer research. A major conclusion was that 72 percent of the customers pick out their store because of the personnel. That might be so, but does he think that if he had the nicest people in the world working for him and much higher prices than his competitors, he would continue to do business? We will grant that if all other factors, including convenience, distance, prices, variety, and everything else, were equal, personnel is the factor that decided where people pick their stores. But all other factors are never equal!

### Five Questions

Thus far I have been telling only about possible errors that appear in figures. It may seem that I am talking against the use of statistics and research, but I am not. The credulous friends of research and statistics have done great damage to their use and acceptance through the misuse or too-ready acceptance of research figures. The important thing is to know what to do when you are faced with a figure.

Darrel Huff has posed five simple questions that you might ask yourself when you need to analyze a figure:

(1) *Who says so?* You may be greeted with a statement like this: "85 percent of all foodstuffs are purchased by women." But you might see another figure that says 35 percent are purchased by men, and still another that says that 25 percent are purchased by teenagers. You know that the stores cannot be doing quite so well as to get up to 145 percent of total sales! Now let us see who made these statements. Oddly enough it was a women's service magazine that brought to your attention that 85 percent were purchased by women, while it was a man's magazine that mentioned that 35 percent were purchased by men. And it was a teen-age magazine that gave figures on teen-age purchases. *Who says so?* That is the first question that I would ask of any statistic that comes across my desk.

(2) *How does he know?* Let me give you one example that occurred when I was the research manager for a food organization. A friend in the advertising business was trying to sell a cooperative advertisement and called to ask me the amount of food milk that is used on cereals. I remonstrated that no one could figure that out, and he suggested that it might be 18 percent. I said that it might be, although I didn't

know. And yet this figure was used in advertising. And less than six months ago, I picked up one of the bulletins that come out to inform retailers about their business and found a statement that 18 percent of the fluid milk was still being used on cereal!

(3) *What is missing?* Information may seem to be over exact or be carried out far past the decimal point. But think about it and wonder whether some figure is missing. When a tooth paste manufacturer advertises that "In seven out of eight cases it prevents decay", do you wonder how many times they made that test? Were they giving you the results of all the tests or the one that came out with the most favorable result? For another example I cite a recent front-page story to the effect that food chain stores have tripled their sales in the last twenty years. Now that happens to be absolutely true, but this statement is misleading in its implications. The missing fact is that the total food business increased in almost that proportion over that period of time and that actually the food chains are doing about the same share of the total food business that they were doing about twenty years previously. If you spot what vital fact is missing, you will not jump to a wrong conclusion.

(4) *Did somebody change the subject?* Some statistical genius recently noted that the gross profit on food chains' non-food items is as much as the total net profit of food chains. From that he leads us to the conclusion that this particular share of the business is accounting for all the *net* profit. If you happen to read that carefully, you saw that he changed the subject. I am afraid that too often we are fooled because we do not notice that switch.

(5) *Does it make sense?* This is a time-honored approach that anyone

can apply, but too many of us are lulled into a false sense of security by the "Scientific Approach" or the exact figure. Watch this especially closely on projections. Some of the projections you might see on the future sales of television sets projected from present sales would mean that every family would have to have several sets in the next ten years. Or in the grocery business we are told that over 38 percent of all purchases are made on impulse, not having been intended when the customer entered the store. But does that make any sense to a groceryman or a husband? Can your wife go 38 percent over her grocery budget? It makes more sense to infer that these purchases were half planned, merely the items that she knew that she would remember and did not write down.

#### **Summary**

Remember then Mr. Huff's five questions when any figure fails to make sense: (1) Who says so? (2) How does he know? (3) What is missing? (4) Did somebody change the subject? and (5) Does it make sense?

Practically all businesses should be run, at least in part, by statistics and reports. Research helps businesses avoid many a costly mistake, but uncritical acceptance of any figure is no favor either to your company or to the man who prepared the figures. Any good researcher or accountant welcomes questions, appreciates a chance to show that his figures are sound. He also likes to have you read those little words in footnotes that tell you what the figures mean. His worst enemy is the man who misinterprets the figures. And it really does not matter whether the misinterpretation was intentional or not. The result is the same: you get the wrong answer.

# A LA CARTE MEALS FOR BABY

By ANNE C. GARRISON\*

*Our latest article on Michigan industries deals with one that always will be (pardon us!) an "infant industry".*

## **Little Consumer with the Big Stomach**

When you consider how little food a baby's stomach holds, you realize that it takes a lot of these feather-weight consumers to make a big impression on the market. It has taken a host of babies to bring the industry of preparing their food from nothing at all to \$200,000,000 in twenty-seven years. The whole story is epitomized in the name Gerber, for it was one of the first of such concerns, while today it is the number one producer. Since it is situated in the Michigan town of Fremont, it is of especial interest to readers in this state.

## **Drudgery with a Difference**

Genius lies in exploiting the possibilities of the obvious. In those days the time was not very long past when pediatricians would say that for the first two years of its life a child needed little but its mother's milk. A start was being made toward more liberal feeding views, and indeed pureed baby-food could be bought: it was a rather obscure item on the drugstore shelf. Most mothers tackled the boring task of mashing their infants' food by hand. Fortunately for the rest of us, one of the mothers who rebelled at this happened to be married to a canner. "Why can't you puree these peas for me at the cannery, Dan?" said Mrs. Daniel Gerber to her husband, as she struggled through the daily chore her pediatrician demanded. The fact that Daniel Gerber undertook to do so was responsible for turning his Fremont Canning Company

into the giant that today dominates the baby-food industry. Behind his closed office door he experimented with mashing peas through a strainer — learning something of the stubbornness of peas, the patience of the young mother, and the problems involved in commercial preparation of this type of food. When he had discussed the new project with his father, Frank, the head of the firm, a limited amount of canned baby food was produced. Mrs. Gerber's problem was solved; and so, though they didn't know it then, was the problem of the prosperous future of the company, the town, and the farming hinterland.

## **Country Full of Customers**

It was early the next year that Daniel Gerber realized the potentialities of his nice little new project. He had accommodated some friends with jars of the prepared food for their children, and now he ventured to discuss the possibilities of a wider market with his family pediatrician in Grand Rapids. He found that apparently the country was full of babies who had been needing prepared baby food! There followed cautious and thorough-going discussions with nutritional experts. When the company was assured that the careful technique of the professional canner could preserve vitamin and mineral values lost in most home preparation, they knew that they had an extremely potent selling point as well as a convenient new product.

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\*Mrs. Garrison is Associate Editor of Business Topics.

**"Genius Consists In —"**

There are lots of definitions of that tricky commodity, genius. To exploit an obvious idea is a fine start, but only that. We like the definition that runs, "Genius consists in a firm application of the seat of the pants to the seat of the chair": in other words, intelligent plugging away at your bright ideas until hard sober work has made inspiration practicable. This aspect was well exemplified up in Fremont. Here now was their product: what were the marketing problems involved? First, the food had to be *available*: this meant selling it *as food*, in the grocery, not as a feeding adjunct, in the drugstore. Simple idea? The trick lies in being the first to think of it.

A survey of the buying habits of mothers verified the idea, and underscored another obvious factor: the mother must be sold on the product. Selling the mother — i.e., winning her faith in your product and keeping it, through the decade or so when she is raising young children — has become the watchword of the company. Anybody can mash peas through a strainer and slap them into a can, but only a company with its eye on that potent marketing expert, the housewife, can keep her coming back for the *same brand*, the one she has learned to trust.

**Famous Infant**

In accordance with its evolving philosophy for getting those peas into young America's mouth, Gerber's started its consistently successful sales campaign. The cans began to appear on grocery shelves, at 15¢ for 4½ ounces, cheaper from the start than the small drugstore ones at 35¢. Right away a barrier was encountered. The grocers themselves were dubious about filling shelf-space with something untried. Where was the *proof* that

mothers wanted this, as the Gerber people insisted? Gerber's now provided the proof.

Turn back to those 1928 *Good Housekeeping* magazines in your mother's attic and find their modest advertisement: 6 introductory cans for this coupon and \$1, plus the name of your grocer. Thousands of responses helped answer the grocers' question, and nationwide distribution was achieved by the end of the year.

To keep the consumer buying Gerber's there was need for a human angle in the company's sales material. What more immediate appeal could possibly be made than by a winsome baby picture on the can and in the advertisements? A number of artists were asked to submit sketches suitable for use; one can imagine the mawkish or overblown qualities many of them thought suitable. Fortunately we are familiar only



Michigan's Most Famous Baby.

with the one selected. It was submitted in exactly the form we see it today; an unfinished charcoal sketch, with the pencilled note: "Is this the sort of thing you have in mind? If so, I will submit a more finished version." The artist was assured it was exactly right and should not be changed in any way. So Gerber's famous baby was born, and symbolizes, even in the looseness of the unfinished sketch, the provocative and wistful charm every mother loves in her own child. Sentimentally, the judges were right — and in this business the right sentiment means sales.

#### Technical Matters

This is not to imply that the technical end of production was not of great importance. A nation-wide market meant not only scientific methods of processing and distributing, but it also reached all the way back to scientific growing as well. There was instituted an entire agricultural program involving close liaison work with growers, county agents, experiment stations and the research facilities of several different departments at Michigan State College.

To keep up with growing competition, variety became important. More fruits and vegetables were added and so was a series of four highly convenient and carefully formulated cereal foods along the line of Pablum, which Mead Johnson had already been manufacturing. Perhaps such foods as these, and the more recent strained meats, have taken even more of the load off the young mother's shoulders. (If Daniel Gerber thought straining peas was a chore, he should have tried scraping a meat patty for a baby, or boiling barley for two hours every day and strain it through a hair sieve for use in a formula). Gerber's of course, has not been alone in the field. The

processors have kept each other hopping in the competition over Baby's economically important supper dish. They have all wanted to hang onto Baby's trade, too, once his teeth are cut, for a lavish line of chopped foods supplements most lines of purees and cereals.

Gerber's latest item, one of its most painstakingly developed, certainly its costliest, is a meat-base formula for cases of milk allergy. A doctor has called it "the best news in twenty years of research into infant feeding." This item is an example both of Gerber's ingenuity in extending its market and of its close cooperation with the doctor and the clinic in developing a product that fills a genuine need. The trend in infant feeding is toward protein at an early age. Meat base formula and the strained meats provide what nutritionists recommend in an utterly convenient form.

#### Everybody Grows

While Gerber's has not tripled its birthweight in a year, as every one of its customers does without even trying, its expansion has been satisfactory indeed. Price has dropped throughout twenty years of rising prices in the economy in general. When baby food became the Fremont Canning Company's chief concern in 1941, the name was changed to Gerber Products Company, and two years later other types of canned goods were discontinued. Thus the firm was enabled to use the catchy and memorable slogan of today: *Babies are our Business: our ONLY Business.*

At the same time, nation-wide demand necessitated setting up a large plant in Oakland, California. A few years later there was evolved an arrangement with Armour whereby it packs strained meats under the Gerber

label and supervision up in Minnesota. An Oregon subsidiary next was opened to add to the output of strained fruits and vegetables, while one in Rochester, New York, recently completed, has made the operation truly nation-wide. Citrus products come from a Florida plant. There is a subsidiary company in Niagara Falls, Ontario, to handle Canadian business.

The line today consists of sixty-three strained and junior foods, all the way from rice cereal to a canned egg-yolk that is the answer to a mother's prayer. The egg-yolks were among the most difficult of the whole series to perfect, involving vexatious problems of taste and texture. One recent product with a humorous connotation is a neat baby-fist-sized teething biscuit, a sort of super-puppy-biscuit for gum-sore humans. These palatable items are hard as granite and brown in color. In evolving this item alone, 97 different formulas were tried, 12 different flours and 20 other ingredients tested. There followed tests in a thousand homes. Only after these returned a favorable verdict did the plant go ahead with production.

#### Filling Baby's Supper Plate

It would take a long article indeed to cover the life history of each of the items manufactured in the Fremont plant. To take only one of these, let us consider the apple, from fruit blossom to the culminating moment when Baby overturns his dish of applesauce onto the cat. First of all comes the selection of the variety of fruit. Market research has shown that the mother, confronted by a row of jars of applesauce in the store, will pick the lightest in color. A whimsical method of selection, no doubt, but Gerber's meets her demand. Consequently they seek a type of apple that will cook to a light uniform con-

sistency, and they buy Grimes Golden or Golden Delicious whenever possible. Gerber's field men inspect the trees, the blossoms, the fruit at every stage of its development, and maintain close touch with growers, fruit experiment stations and experts of all kinds in order to insure maximum quality in the fruit, which is only the raw material for the finished product. From the time the barrels of ripe fruit are rolled out onto the plant's receiving platform, specially trained Quality Control men follow it through every step of processing, constantly vigilant to detect, by every means from spot checking to X-ray, conditions that might endanger the high standard of the finished food.

No conscientious mother could possibly handle a fresh apple for baby with the care given to these. In washing, coring and splitting, they are not touched by bare hands. They are steam-cooked in a continuous-flow cooker from which air is excluded to retain the greatest possible amount of vitamins and minerals. The sauce is strained, slightly sweetened, laboratory tested for flavor, and all this while is handled only by scrupulously clean stainless steel. Some of the product is packed in tin, some in glass, the method of final handling varying accordingly. As to the merits of tin versus glass, processors find tin a little easier to handle, with lower loss from breakage, but due to a long-standing prejudice in favor of visibility, and against the "poisonous" quality of tin,\* most mothers prefer glass.

Packed, sterilized, cooled in transit through a long tank of water, the containers are not only washed and dried, but polished. They are then labelled on

\*A tin can is not tin, nor does it carry any risk of tainting the food—but try to combat a prejudice!

fiendishly ingenious machines that operate too fast for the eye to follow and subjected to X-ray inspection. The finished food containers are packed for shipment throughout the United States and Central and South America. Similar painstaking treatment, varied in accordance with conditions, prepares everything else from vanilla pudding to carrots. Every step of the process is subject to constant checking and testing, not only for quality but for efficiency of packing methods, safety of operation from the worker's point of view, and economy in handling.

#### **Agricultural Economics: an Interesting Angle**

In the field of Agricultural Economics there are many triumphs to be recorded to the score of the commercial processors and their state-supported or private research associates, and some knotty problems remain to be ironed out between growers and processors. Basically, the problem involves the divergent needs of the fresh fruit grower versus the grower of fruit for processing. To take one example, let us consider the growth of peaches in Michigan. Freestone peaches developed in Michigan (a whole family descended from trees at the South Haven experiment station of Michigan State College) can greatly extend the peach grower's harvesting season and give him a balanced crop likely to yield a good return on the retail market. Ideally, he would like to diversify, and sell some to the buyers of fresh fruit and some to the processor. He likes to feel that he can count on fresh sales primarily, for in good years (the ones he prefers to remember) fresh fruit sales bring considerably more than the processor can pay him (it costs money to run fruit through all that machinery

and into a can, and most of the processor's expenses are fixed).

Now the processor has different ideas about what he wants in fruit. Handsome appearance in the raw means little to him: he wants firmness, a fair degree of uniformity, and other factors making for ease of handling, and attractiveness in the finished product. Certain fruits have been deliberately developed to fill his needs: in peaches, the one he wants is Ambergem, a clingstone. He would be happy to have all the growers concentrate on Ambergem. But it takes years to bring an orchard to production; Ambergem is useful only for processing; the processor, while desiring this type exclusively is reluctant to offer contracts to the growers, because of uncertainty of prices in his own highly competitive business. And growers, understandably, are reluctant to "convert" to Ambergems without a contract.

Both sides have a distinct point of view, and caught in the middle is the state research man and the county agent, for as public servants they are attempting to help both sides of this unresolved problem, and the public at large as well. The optimistic angle of the difficulty is that both sides are aware of their problem and are working on it. In the words of one grower, "With understanding of each other's problems and a more cooperative attitude on the part of both, I believe we will see the day when many growers will have made the processor their first choice for marketing their fruit."

#### **Opportunity in Apricots**

Apricots, inoffensive and pretty as they look, are a big headache to the processor. There is no commercial growth in this state, for though the tree is hardy enough, it blossoms too early to be safe from frost. Its insect

enemy the curculio beetle has been licked by a new insecticide, methoxy-chlor, and the search for later-blossoming varieties that will make possible growing on a commercial basis is being vigorously pursued by Michigan State College experimenters. For some time they have been making inquiries throughout the state for pet back-yard apricot trees that have borne fruit, and when they discover such trees they take cuttings from them.\*

For reasons of climate, soil, or grower's reluctance, many needs of processors such as Gerber's still have to be met outside the state. A list of the percentage of requirement of each favored variety that is obtained by Gerber's local plant *in state* follows:

Apples (Grimes Golden and Golden Delicious) 65—70%

Pears (Bartletts) 50—75%

Peaches (Ambergem) 5—10%

Plums (Stanley) 75%

The implication seems to be that if Michigan fruit growers can be persuaded to shift to varieties that will benefit the processor, an almost unlimited amount of Michigan fruit can go to market this way. However, it remains a difficult problem to make the shift profitable for the grower.

At the present time, half of the state's vegetable crop is processed. Gerber's offers contracts to its growers of peas, spinach, green beans, squash, and sends out its own viners and cutters to handle these products right in the farmers' fields.

#### New Aspects and Developments

It might be supposed that the practice of freezing foods today would endanger the position of the canning industry. This seems not to be the case

\*As apricots have the highest vitamin A content of any commonly grown fruit, they are much in demand for baby foods.

as regards baby foods, for the convenience and permanent availability of the can or jar makes it secure in the housewife's preference, in the opinion of Gerber's. They also feel that their product, once in its container, is under more stable conditions than if it were frozen.

As our population steadily ages and the needs of seniors begin to get attention as well as those of juniors, the science of geriatrics comes more and more into the medical picture, and with it the dietary needs involved. Gerber's products and similar ones of other firms can fill many of these needs. Consequently, while aware of this growing market, the firm does not plan to modify its products to meet it. In their present form they provide great variety, and their very blandness makes them capable of interesting variations to suit the adult taste.

#### Factory and Community

From Gerber's first days as the Fremont Canning Company, the founder, his son and grandson have all been acutely aware of the obligation of their establishment to the community. In one respect the problem of such relationship was particularly prominent in the days when the plant carried on only seasonal operations, like most canneries. This meant, of course, a lot of work in one period, none at all the rest of the time, with a resulting dislocation of the stable rhythms of life in home, town and factory. The possibility of converting the plant to its present type of operation, whereby 800 people are employed 42 hours a week throughout the year, was a prominent factor in the decision to concentrate in the processing of baby foods. The result has been mutually beneficial. Many employees have been with Gerber's twenty years and more, and you will find families in which several members

and two or three generations are all Gerber's workers, or have been. The town at large has enjoyed the diffuse and indefinable benefits of this type of stability — it is no exaggeration to say that even the casual visitor driving through the main street senses this atmosphere of economic well-being, as he does perhaps in no other Michigan town to the same degree, with the exception of Midland.

The benefits extend, of course, to the countryside. Assurance of a steady market for vegetables and fruit, constant encouragement and cooperation in upgrading quality of produce, long-standing friendly relations with the firm — all these contribute to the stability of agriculture throughout the

area, reflected in enlarged landholdings and diversity of crops.

The story of Gerber's is practically the story of the Michigan baby-food industry, with the exception of milk formula products of Wyeth (in Mason) and Mead Johnson (in Zeeland). These fall into a different category, and have been touched upon in a previous article on Michigan pharmaceuticals.

My thanks are extended to Stephen S. Nisbet and the research department of the Gerber Products Company, Fremont, Michigan; to H. B. Tukey of Michigan State College; to Stanley Johnston of the South Haven Experiment Station; and to Floyd Fox of Shelby for the background material on which this article is based.

### a 20th Century Fact



Families with children tend to have better diets than those without children, notes a forthcoming Twentieth Century Fund report. This is so even though their average income is no higher and they have more persons to feed.

*(Courtesy of the Twentieth Century Fund)*

# THE BLOCKAGE FACTOR IN STOCK VALUATIONS FOR FEDERAL TAX PURPOSES

By A. E. GRUNEWALD\*

*Probably not many of us are embarrassed by the legal difficulties brought about by the inheritance of large blocks of stock. The question, however, has come up often enough to have received a good deal of attention as regards interpretation of the law involved. Mr. Grunewald's thorough-going consideration of the topic will be helpful to anyone faced with this situation.*

Where corporate shares are listed on an organized stock exchange and actively traded, the quotations for the shares on the valuation date will usually be taken as conclusive evidence of the "fair market value" of the shares for federal tax purposes.

However, the taxpayer may be able to establish that what might be the "fair market value" per share of a small block of stock does not represent the "fair market value" per share of a much larger block of the same stock. This is the question of the relevance of the blockage rule in the determination of the "fair market value" of listed and actively traded corporate shares for federal tax purposes.

*The Blockage Rule* — It is readily apparent that the dumping of a large block of stock on the market at one time would reduce the per share price if there were not present in the market sufficient willing buyers to absorb the shares offered at the previous per share price. One attorney illustrated the blockage rule as follows:

To illustrate the Blockage rule let us say that Smith dies in possession of a painting by an old master on which a valuation of \$1,000,000 is placed. His neighbor

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Jones also dies, but has ten paintings by the same master. If the court should decide that the paintings belonging to the late Jones were worth only \$90,000 each because if offered as a group they would momentarily glut the market and weaken the price structure, it would be employing the Blockage rule.<sup>1</sup>

Clear cases where an allowance for blockage is justified may consist of either where a very large block is involved such as in *Helvering v. Maytag*,<sup>2</sup> where the number of shares in the block was twice the amount held by the public, or as in *Jenkins et al. v. Smith*,<sup>3</sup> where, though the block of stock was relatively small, consisting of only 3 percent of the shares outstanding, yet the market for the stock was exceedingly thin; less than .0003 percent of the shares being traded in any one day. Between these two extreme cases almost any variety of circumstances is possible.

In *Helvering v. Maytag*, the issue at bar was the "fair market value" of 133,000 shares of common stock of the

<sup>1</sup>Harvey W. Peters, "The Fair Value of Stocks" vol. 17 *Taxes* Jan., 1939, p. 18.

<sup>2</sup>215 F. 2d 55 (8th Cir. 1942), *cert. den.* 316 U.S. 689 (1942), (e.g.t.). The cases cited are identified in the following manner: income tax, i.t., estate tax, e.t., gift tax, g.t.

<sup>3</sup>21 F. Supp. 251 (D. Conn. 1937), (e.t.).

Maytag Company for estate tax purposes and 400,000 shares of common stock of the same company for gift tax purposes. The Board had given due weight to the size of the blocks of stock involved. The Circuit Court of Appeals upheld the Board in the following language:

As well as any controversial question may be settled without a declaration of the Supreme Court, it is established that the size of a block of listed stock may be a factor to be considered in its valuation for gift and estate tax purposes.<sup>4</sup>

In *Jenkins et al. v. Smith*, the issue at bar was the "fair market value" of 17,679 shares of American Home Products Co. stock on November 1, 1934. Transactions in the stock had taken place at \$31.50 per share on October

31, 1934, and at \$32.00 per share on November 2, 1934. The Commissioner of Internal Revenue attempted to sustain a value of \$31.25 per share for the stock on the valuation date. The plaintiff contended that on the valuation date the shares could not have been sold for more than \$30.00 per share because of the exceedingly thin market which existed for the shares at that time. In support of this contention, the plaintiff introduced expert testimony to show that the block of stock could not have been sold on the exchange on the valuation date without materially depressing the market price. In order to dispose of the shares a private sale would be necessary, and that to thus dispose of the shares they would have to be sold at from 1 to 2½ points below the existing market price

<sup>4</sup>125 F. 2d 55, 63.

TABLE 1\*

CASES INVOLVING THE BLOCKAGE RULE IN WHICH A VALUE BELOW THE QUOTED MARKET PRICE FOR THE SHARES HAS BEEN FOUND.

Case	Number of Shares In Block	Quoted Market Value	Fair Market Value found by the court or the Board	Percentage Reduction
Girard Tr. Co., (B.T.A. .... Memo. 1937), (e.t.)	134,968	\$114.00	\$70.50	29.3%
Groff v. Smith, (32 .... A.F.T.R. 1659, aff'd 150 F.Supp. 2d 825), (g.t.)	14,000	23.375	21.50	8.0
Havemeyer v. U.S., (59 .... F.Supp. 537, cert. den. .... 326 U.S. 759), (g.t.)	160,000 20,000	28.125 24.50	25.00 22.00	10.7 10.2
Jenkins v. Smith .... (21 F.Supp. 251), (g.t.)	17,679	31.50	30.00	4.8
Kimberly: Helvering .... v. (97 F. 2d 433), (g.t.) ....	30,000 18,000	12.125 15.00	10.00 11.00	17.5 26.6
Knoblock v. Smith .... (25 F.Supp. 156), (e.t.)	14,778	19.00	15.00	15.8
Shattuck: Comm. v. .... (97 F. 2d 790), (g.t.) ....	30,000 10,000	13.00 10.00	10.00 7.50	23.1 25.0
Sherr v. Comm. .... (T.C.M. 1951), (g.t.)	14,000	8.00	7.00	12.5
Vits, (B.T.A. Memo. .... 1940), (e.t.)	77,294	10.00	8.00	20.0
Whitmore, (B.T.A. .... Memo. 1938), (e.t.)	28,020	24.625	21.00	18.8

\*Source: Based on *Montgomery's Federal Taxes, Estates, Trusts and Gifts*, 1951-52, pp. 664-65.

quotations. The court upheld the plaintiff.

The size of the blocks of stock involved in the blockage controversy and the extent of the discounts granted for blockage may be seen in the table presented below.

*Treasury Policy* — The policy of the Treasury concerning the question of blockage has wavered. As early as 1919, Regulation 37 contained a clause which prohibited any allowance or discount for the size of the block of stock under consideration. Subsequent regulations down to 1934 were silent on the matter. In the period prior to 1934 administrative practice wavered and there was some tendency to grant an allowance for blockage if the point was sufficiently stressed.

The first case wherein the question of blockage arose was tried in a state court. The court in *Bingham's Administrator v. Commonwealth*<sup>5</sup> refused to allow a discount for blockage on the ground that such an allowance would institute one method for the rich man and another for the poor man for the same property on the same day. Some of the early state and federal courts, however, gave limited recognition to the blockage theory, though none can be clearly cited as supporting the blockage theory.

In 1934 the federal estate tax regulations were modified so as to expressly exclude any allowance whatever for blockage, and shortly thereafter the federal gift tax regulations were likewise modified.

Writing in 1937, Professor Bonbright concluded that the weight of authority was against any allowance

for blockage<sup>6</sup> and that the "fair market value" of a block of listed and actively traded stock was to be determined on the basis of the current market price quotations without any discount for the size of the block.

In recent years, however, there has been a more favorable attitude toward acceptance of the blockage theory and substantial discounts have been allowed in a number of cases, as shown in Table 1.

In the leading case of *Safe Deposit and Trust Co. of Baltimore v. Commissioner*, the Board of Tax Appeals, though refusing to allow any mechanical application of the blockage rule, nevertheless gave due weight to the size of the block of stock involved and lent qualified support to the blockage theory in the following language:

This conclusion has not been arrived at by any dogmatic recognition or non-recognition of any so-called 'blockage rule' . . . 'Blockage' is not a law of economics, a principle of law or a rule of evidence. If the value of a given number of shares is influenced by the size of the block, this is a matter of evidence and not a doctrinaire assumption.<sup>7</sup>

The Commissioner appealed, but the Circuit Court of Appeals in *Helvering v. Safe Deposit and Trust Co.*, upheld the Board in the following language:

In our opinion the Board was right in basing its conclusions upon the realities as it found them rather than upon considerations of abstract logic. It could not ignore the pregnant fact, having found it to exist, that a large block cannot be marketed and turned into money as readily as a few shares.<sup>8</sup>

In 1939 the regulations were modified so as no longer to preclude the

<sup>5</sup>196 Ky. 318, 244 S.W. 71 (1922), (e.t.).

<sup>6</sup>735 B.T.A. 259 (1937), (e.t.).

<sup>7</sup>895 F. 2d 806 (4th Cir. 1938), (e.t.).

granting of a discount for the size of the block to be valued,<sup>9</sup> and in 1942 the Bureau of Internal Revenue reluctantly accepted the blockage rule when *ceteriorari* was denied in *Helvering v. Maytag*<sup>10</sup> and *Phipps v. Commissioner*.<sup>11</sup>

The applicable federal estate and gift tax regulations at present provide:

In cases in which it is established that the value per bond or share of any security determined on the basis of selling or bid and asked prices as herein provided does not reflect the fair market value thereof, then some reasonable modification of such basis or other relevant facts and elements of value shall be considered in determining fair market value.<sup>12</sup>

However, the blockage rule cannot be applied in a random and haphazard manner. Care and judgment must be exercised in determining whether or not an assertion that a discount be granted because of the size of the block will stand analysis. It must be justified by the facts and not based on mere opinion.

The increase in secondary distributions in recent years of large blocks of previously issued stock may be one of the factors which has been responsible for the wider acceptance of the validity of the blockage rule by the courts and the Bureau of Internal Revenue where before the applications for such discounts were generally rejected. If blockage was not rejected, the determination of its exact amount was relegated almost entirely to the realm of pure guesswork. This is no longer true today. Secondary distributions through

<sup>9</sup>Reg. 80 (1937 ed.) Art. 10 (a) as amended by T.D. 4902 (C.B. 1939-1, I, 305).

<sup>10</sup>125 F. 2d 55 (8th Cir. 1942) *cert. den.* 316 U.S. 689 (1942), (e. g. t.).

<sup>11</sup>127 F. 2d 214 (10th Cir. 1942), *cert. den.* 317 U.S. 645 (1942), (g. t.).

<sup>12</sup>Reg. 105, Sec. 81.10 (c). Reg. 108, Sec. 86-19 (c).

underwriters and brokers have been uniformly accepted as an economical means of liquidating large holdings of shares and have substituted what was previously almost entirely pure guesswork for a fairly easily determinable minimum cost of disposing of large blocks of shares. And both taxpayers and the Bureau of Internal Revenue have usually found this method acceptable.<sup>13</sup>

Taxpayers have not uniformly contended that a large block of stock was worth less per share than a small block of similar shares. When it has been to their advantage they have contended that the large block of stock was *more* valuable per share, for purposes of control, than a small block.

*Applicability of the Blockage Rule*  
— Until a number of years ago the Commissioner of Internal Revenue vigorously opposed the application of the blockage rule. However, he was forced to abandon this uncompromising position by subsequent court decisions which have held that he could not, either by rule or by regulation, limit the evidence which is to be considered in any given valuation case. It is now well established that the size of the block of stock is a factor which is to be considered and both the regulations and the cases sanction the blockage rule.

The taxpayer, however, is not entitled to an unqualified and blanket allowance because of the mere fact that the block of stock involved in the valuation dispute is relatively large in relation to the number of shares normally traded or the amount traded during the period surrounding the valuation date. *Prima facie*, the market price quotations prevailing on the critical day will control unless the taxpayer is able to

<sup>13</sup>Roger K. Powell, "Estate Tax Valuation", *Estate Tax Handbook*, ed. J. K. Lasser, Mathew Bender & Co., Inc., N.Y. 1951, p. 385.

establish to the satisfaction of the court that the block of stock could not have been sold within a reasonable period of time at the prevailing market price quotations which existed on the material date. A mere showing that the block of stock is large in relation to the volume traded is not enough. Many taxpayers have failed to prevail before the Board of Tax Appeals, the Tax Court, and the federal courts because they have rested their case solely upon the testimony of expert witnesses who contended that a discount for blockage should be allowed *merely* because the size of the block in question was large in relation to the number of shares traded, but failed to substantiate their testimony with facts and figures. The position of the taxpayer, generally, is better the more complete the testimony and the more fully it is supported by relevant data. One must not fail to remember that each valuation case is different, that each case is largely a question of fact, and most important, that the burden of proof must be borne by the taxpayer.<sup>14</sup> In the absence of a contrary showing the valuation of the Commissioner will be sustained.

Various other factors may be of material consequence in supporting a plea for a blockage discount in addition to the factor of the size of the block in relation to the number of shares normally traded and the number traded on the critical date. Such factors as the value of the block of stock in question, the frequency with which the stock is

traded and the importance of the very stock exchanges upon which the stock is listed may carry controlling weight.

The direction of the trend is often a controlling factor. If after the valuation date, the stock rose steadily in price, it probably would be difficult to convince the court that the stock could not have readily been sold within a reasonable period of time at the market price quotations prevailing on the material date. On the other hand, if the stock was listed and actively traded, the block large in relation to the number of shares normally traded, and in addition, the market price for the stock declined subsequent to the valuation date, it would be reasonable to predict that the court would grant an allowance for the size of the block. If subsequent to the valuation date the market price for the shares remained relatively stable, the other factors such as the size of the block in relation to the number of shares traded, the value of the block in question, and the demand for the stock by investors will be controlling. Nevertheless, though some of the above factors may presage an allowance for blockage, it is not certain that the court will grant it in all cases. In *Bull v. Smith*,<sup>15</sup> the Circuit Court of Appeals suggested that the blockage rule does not apply and no allowance for blockage will be granted where, within a reasonable period of time, an adroit broker could have realized the amount established by the Commissioner as the "fair market value" of the shares.

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<sup>14</sup>Dobson v. Comm., 320 U.S. 489 (1943), *reh. den.* 321 U.S. 231 (1944), (i. t.).

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<sup>15</sup>119 F. 2d 490 (2nd Cir. 1941), (e. t.).

#### ANSWERS TO "DO YOU KNOW THESE MICHIGAN TOWNS?"

(From page 5)

1. Zeeland; 2. Mt. Pleasant; 3. Grant; 4. Bay City; 5. Morelia, Michoacán, Mexico. We put this in to make you feel bad. Name of the state is almost the same, at least.

## Meetings of Unusual Interest

Two symposia at Michigan State will bring authoritative speakers to the campus on some of the greatest problems of business. (A "symposium" is a gathering at which several people contribute their ideas on a subject.) Everyone is welcome to attend these symposia, with no charge except for meals. Those who wish to stay overnight may make reservations at Kellogg Center.

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April 12 and 13. Sponsored by the School of Business and Public Service.

During the day of the 12th there will be individual sessions in each of the following fields:

• Accounting	Marketing
Business Education	Management
Economics	Hotel, Restaurant and
	Institutional Management

A panel representing management and labor on the morning of the 13th will discuss: "Automation: What It Is and What Is Coming." Also four major addresses will be given by nationally prominent executives. Since both specialized areas and questions of broad business interest will be treated by outstanding men, this symposium holds value for anyone concerned with business.

For detailed information and reservations write to: Division of Business, Michigan State College

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For detailed information and reservations write to: School of Engineering, Michigan State College

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### RESEARCH REPORTS

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7. *Michigan Tourist Survey (Free)*
8. *Monroe Industrial Survey (Free)*
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